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BRIEFS AND COMMENTS

EGYPT-USSR: Conciliatory Gestures

//Egypt recently has made some tentative gestures toward reducing the hostility in its relationship with the Soviet Union. A significant breakthrough in the near term, however, is highly unlikely. [redacted] 25X1

In a speech on 15 May, President Sadat accused Moscow of instigating anti-Egyptian moves by other Arabs but also stated that Egypt was willing to "reciprocate friendship for friendship." Sadat made a similar remark to a group of French journalists earlier this week. [redacted] 25X1

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//Egyptian officials probably hope that such offers will help lessen Soviet opposition to Egyptian-Israeli negotiations and to the continued use of a UN force in the Sinai. They may also calculate that even a hint of movement toward better relations with the USSR would encourage some Arabs to consider a less hostile policy toward Egypt. [redacted]

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//Sadat's suspicions about Moscow's intentions toward him personally run deep, however, and this will make normalization efforts extremely difficult. In a move that in part reflects Egyptian apprehensions about the USSR, Egypt's Interior Minister on Thursday publicly expressed suspicion that the Soviets were involved in a recently terminated Bulgarian intelligence operation in Egypt.// [redacted]

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The Soviets would welcome some improvement in relations with Egypt, but they think they must avoid appearing too eager because of the hostile reaction of the radical Arab states. It is unlikely, in any event, that any bilateral progress between Moscow and Cairo would affect Soviet opposition to the Egyptian-Israeli peace treaty. [redacted] 25X1

[redacted] 25X1

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CHILE: Improving Economic Picture

Increased exports, the continuing inflow of financial credits, and new direct investments have improved Chile's economic prospects. Chile's stronger payments position has enabled it to expand imports, initiate new investments, and build international currency reserves.

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Rising copper prices and surging agricultural, fishery, and forestry exports will enable Chile to improve its current account deficit, which has increased sharply since 1976. We expect Chile's trade deficit will be cut in half this year and thereby more than offset rising interest payments. In turn, the current account deficit probably will decline by 15 percent to $700 million in 1979. [redacted] 25X1

Private capital inflows this year will likely amount to $1.8 billion, only slightly below last year's record total. Backed by its current excellent international credit rating, Chile recently arranged $350 million in new credits during the first quarter. Although US banks managed the bulk of the loans between 1976 and 1978, Chile this year has aggressively moved to tap non-US financial markets and has been increasingly successful in garnering official loans, which had fallen sharply in recent years. Chile has also secured new lines of supplier credits, mainly from non-US banks, to finance soaring import requirements. [redacted] 25X1

Direct investment by foreign corporations is increasing, with natural resource projects attracting the bulk of the new funds. Direct investments are likely to total $300 million this year--twice last year's level--as US corporations continue to increase their stake in Chile.

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The rapid inflow of private capital in the first three months of this year will probably slow by the end of the year because burgeoning foreign exchange inflows are undermining government attempts to reduce inflation. Last month, Santiago imposed reserve requirements on foreign borrowing to slow heavy borrowing and a growing debt service burden. Chile's external debt now totals $6.9 billion--60 percent of its gross domestic product.

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CHINA-JAPAN: Renegotiating Plant Contracts

China appears ready to reinstate a large portion of the $2.4 billion in Japanese plant contracts it suspended in February. An agreement reportedly has been reached on the $1 billion in stalled contracts associated with the Baoshan Steel Mill, and talks on the 20 suspended petrochemical contracts are proceeding on a contract-by-contract basis. The Chinese are pushing to have the contracts reinstated on a deferred payments basis rather than on a cash basis as agreed to under the initial contracts.

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UNCTAD: Developments at the Conference

The fifth session of the UN Conference on Trade and Development--now moving into its final week--probably will yield many resolutions but few of them are likely to result in much action. There have been no new proposals attractive to large numbers of developing countries, and there is a widespread sense that the time is not ripe for new initiatives on resource transfers. Major blocks at the session have been vulnerable to internal dissension and to attack from other groups. All sides are seeking to wind up the conference without diplomatic embarrassment. [redacted] 25X1

Most industrialized countries are still dodging demands by the developing countries for adherence to aid targets, for specific pledges to the Common Fund's commodity development program, and for a reopening of the Multilateral Trade Negotiations. The Communist countries are trying to deflect attacks from the developing countries over their low levels of trade and aid by raising East-West trade issues, and by charging that the industrialize West has done little to help the developing countries. The developing countries are less tightly organized this session than they have been in the past, but they are seeking to preserve sufficient unity to gain commitment from the industrialized nations to a few of their proposals. [redacted] 25X1

//The biggest suprise of the conference occurred when Costa Rica and other Central American countries broke longstanding taboos among the developing countries by introducing the international energy issue. Despite blandishments from members of the Organization of Petroleum Exporting Countries, the Central American countries refused for more than a week to continue talks in a key negotiating group until OPEC members agreed to discuss the energy problems of the developing countries that depend on oil imports. [redacted] 25X1

25X1 [redacted]

25X1 [redacted]

POLAND: Prime Minister's Health

Premier Piotr Jaroszewicz reportedly is recuperating from a mild heart attack. His illness will give new impetus to long standing rumors that Jaroszewicz, a member of the ruling team since Gierek came to power in December 1970, might be replaced because of the country's difficult economic problems. The 69-year-old Jaroszewicz, who has a history of medical problems, is closely associated publicly with Warsaw's ill-fated effort in 1976 to raise prices and with subsequent economic stringencies. Jaroszewicz has shown considerable political durability, suggesting that his reputation for being trusted by the Soviets is well grounded.

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SPECIAL ANALYSIS

SOUTH AFRICA: Shaky Economic Expansion Continues

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South Africa's fragile economic upturn of the past 18 months, which follows three years of declining growth rates, will probably continue for the rest of 1979. Expansion this year will be less rapid than the governments's 4-percent goal, however, because of the cutoff of Iranian oil, lagging consumer demand, and continued capital outflows. 25X1

The economic troubles of the past five years began with government overreaction to soaring gold prices and to strong domestic growth in 1974. Buoyed by these developments, Pretoria embarked on massive development spending to expand exports and increase self-sufficiency. The onset of serious economic problems, however, caused South Africa to suffer record current account deficits in 1975 and 1976 and steep increases in capital outflows in 1977 and 1978. 25X1

-- South Africa lost an estimated $1.3 billion a year in foreign exchange because of declining prices and production of gold.

-- South Africa increased defense spending by 74 percent over two years in response to the introduction of Soviet-backed Cuban troops in Angola in 1975.

-- South Africa's standing in international investment and lending markets was undermined by the racial riots in 1976 and by the intensified international pressures for South African action on the Rhodesian and Namibian issues. 25X1

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Despite balance-of-payments and financial constraints, government expenditures rapidly increased through 1977, reflecting both military expansion and a push to meet construction timetables on import substitution and export-related projects. Pretoria sees both reduced reliance on imports and heightened Western dependence on South African raw materials as protection against the threat of future international sanctions. Most of the $24 billion in projects already on the slate in early 1977 bore on this goal, particularly projects for the expansion of electric power and steel output, coal liquefaction, and interrelated harbor, railroad, and mining improvements. 25X1

In its effort to strengthen the balance of payments, South Africa concentrated on dampening private domestic demand to reduce imports. Tight monetary and fiscal measures curbed private consumer expenditures from a growth of 6.2 percent in 1974 to a 0.6-percent contraction by 1977. With demand falling, manufacturing, construction, and domestic trade declined by 5 to 6 percent in 1976 and 1977. Investment plummeted as the industrial capacity untilization rate declined to barely more than 80 percent. Only mining and agriculture showed production increases. The net result was a decline in real growth from 8.2 percent in 1974 to 0.2 percent in 1977.

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An upturn in the foreign sector of the economy pushed total output up by a moderate 2.5 percent in 1978. Exports climbed at an average annual rate of 11.5 percent in 1977 and 1978 after stagnating in 1975 and 1976. Nongold exports rose dramatically, benefiting from the completion of large government coal and iron ore export projects, high international prices for diamonds, and unexpectedly high iron and steel shipments. Last year, gold earnings jumped 38 percent to an alltime high of $4.2 billion. With only a mild pickup in imports, the surge in exports yielded a record current account surplus in 1978 of $1.6 billion. 25X1

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The post-1974 slowdown in the private sector and political uncertainties have steadily reduced direct foreign investment in South Africa. Net private foreign investment--which amounted to $457 million in 1975--turned negative in 1976, and by 1978 the net outflow had reached $1.3 billion. Heavy short-term borrowing from overseas currency markets have maintained international reserves at not less than three months worth of imports. As a result, private international bank claims on South Africa have tripled since the end of 1974, to more than $8 billion. [redacted] 25X1

Economic growth in 1979 will probably exceed last year's 2.5 percent but is unlikely to reach the 4-percent goal of the Botha government. This moderately bullish projection faces more downside risks than upside possibilities. [redacted] 25X1

Gold again is turning out to be a key strong point for the economy. Downward pressures on gold prices, anticipated earlier because of sales by the US and the International Monetary Fund, have been softened by US Treasury decisions to reduce offerings and by the impact of the tight international oil situation on investor perceptions of inflation prospects. Gold prices so far this year have averaged approximately $240 an ounce compared with $195 in 1978; every $10 change in price means $230 million--on an annual basis--in foreign exchange earnings for the South African Reserve Bank. [redacted] 25X1

The 1980 budget, submitted last month, reflects a determination to reduce the role of government in the economy, and government spending will probably not be a major source of economic stimulus. The real rise in expenditures has been set at only about 1 percent; funding of self-sufficiency and export projects will continue to receive high priority. The budget includes $950 million in tax cuts on individual and corporate income, reduces a longstanding surcharge on imports of consumer goods, and makes cautious changes in budgetary financing to accelerate the growth in money supply. [redacted] 25X1

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Steep fuel price increases, however, plus rises in administered prices for staple foods, such as corn, are likely to reduce the real effect of the budget stimulus. Most of the tax relief, moreover, is focused on middle and upper income whites, who are more likely to put increased take-home pay into savings, thus dulling the impact on demand. 25X1

Without a strong upturn in consumer demand, a reversal in capital outflow before the end of the year seems unlikely. The tax cuts will not be implemented until July, and even a subsequent sharp pickup in private consumer demand would hardly be translated into promising opportunities for direct foreign investment before the end of the year. The lack of a rebound in private investment outlays would blunt the impact of new incentives announced in January to attract foreign investment. The incentives consist of a phased removal of antiquated constraints on capital repatriation. So far, the Reserve Bank's cautious implementation of the reforms has bred uncertainty among investors over the extent and kind of opportunities to be expected. 25X1

Drought since late 1978 also has depressed growth and balance-of-payments prospects. We now estimate the key corn crop at 6.5 million tons, contrasted with last year's 9.9 million tons. Corn exports during this marketing year will drop steeply, therefore, from about 3 million to less than 1 million tons. 25X1

Prospects for continuing steep increases in oil costs will also restrain economic expansion. South Africa has no oil wells of its own. The cutoff last December of oil exports by Iran, which had been supplying 80 to 90 percent of South Africa's crude imports, has forced refiners to purchase oil on the spot market by way of third and fourth party transactions; the oil import bill will be pushed up about 50 percent to \$2.4 billion to \$2.6 billion. Consumer fuel prices have already soared 30 percent this year, and the government is reported to be on the verge of sharply tightening longstanding rationing measures.

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